

The Prevention of Debt Bondage with Microfinance and Related Services: Preliminary Lessons

Patrick Daru and Craig Churchill
International Labour Organization, Social Finance Programme

Numerous South Asian workers are bonded to their employers, forced to work for substandard or no wages because their earnings are retained by the employer to repay an outstanding debt. Debt bondage is most common in the agriculture sector, although it can also be found in other industrial sectors such as mining and gem polishing, brick-kilns, carpets and textiles, as well as domestic service. The victims of bonded labour tend to be the poorest and least educated segments of the population, from low castes and religious minorities.

In 1998, the International Labour Organisation (ILO) adopted the Declaration on Fundamental Principles and Rights at Work, under which all member States have an obligation to respect, promote and realize the elimination of all forms of forced labour.¹ To help member States to abide by the Declaration, the ILO moved from the usual report based supervisory mechanisms to a more proactive approach with a variety of technical cooperation projects designed to prevent forced labour or to help rehabilitate labourers who have been released from bondage.

Starting in June 2000, one such initiative, the Dutch-funded South Asian Project for the Prevention of Debt Bondage, began piloting microfinance-based schemes for the prevention of bonded labour and the rehabilitation of former bonded labourers in four countries, Bangladesh, India, Nepal and Pakistan. This paper describes some of the project's lessons learned during its first 18 months, with a particular focus on: a) an increased understanding of different bonded labour phenomena in South Asia, and b) operational insights that should lead to an improved project implementation.

Understanding Bonded Labour in South Asia

Bonded labour can be somewhat difficult to pin down since definitions and perspectives vary. While significant progress is being made regarding the legal definition, in practice debt bondage is quite dynamic. Although there are examples of bondage that are for short-term and are not particularly exploitative, these are often first steps toward more severe forms of bondage.

Definition of Debt Bondage

International and national definitions. **Forced labour** is a service for which the worker has not offered him/herself voluntarily, and that s/he has to perform under the threat of a penalty (ILO Convention 29 on Forced Labour). The 1956 Supplementary Convention Against Slavery defines **debt bondage** as the combination of a credit and a labour contract in which the value of labour services as reasonably assessed is not applied towards the liquidation of the debt (e.g., only interest is repaid by the labour but principle is never repaid) or if activities

¹ There are four categories of Fundamental Principles and Rights at Work. Besides forced or compulsory labour, the Declaration also covers: 1) freedom of association and the right to collective bargaining; 2) the elimination of child labour; and 3) the elimination of discrimination in employment or occupation.

are neither defined nor limited (e.g., the labourer can be required to work at any time day or night).

The four countries involved in this project have ratified both above-mentioned treaties, so the definitions they contain are applicable to the national context. In addition, related national legislation enacted in three countries includes further descriptions of bonded labour, as summarised in Table 1.

Table 1: National Definitions of Bonded Labour

Country	National Law	Definition
India	Bonded Labour System (Abolition) Act, 1976 (amended in 1985)	Bonded labour is caused by a debt or by social customs and results in restriction of freedom of movement, and/or Restriction of freedom to look for alternative employment, and/or reduction wages and/or product prices
Nepal	Kamaiya Labour (Prohibition) Act, 2001	Kamaiya labour is caused by a debt and results in payment of low wages. It also includes abusive traditional forms of labour.
Pakistan	Bonded Labour Act, 1992. Bonded Labour System (Abolition) Rules, 1995	Bonded labour is caused by a debt or by social customs and results in restriction of freedom of movement, and/or Restriction of freedom to look for alternative employment, and/or reduction wages and/or product prices

Local and traditional systems. International and the national definitions have different scopes and outreach, and have been subject to different interpretations in the field when it comes to identifying whether a person is bonded or not. More practically, local systems of bondage have developed over time with characteristics and types of exploitation that are well known to both employers and labourers, such as in Nepal (Kamaiya, Haliya), Pakistan (Hari) and India (Jeetham, Gothi).

Under this project, the main focus is on economic forms of bondage primarily emerging from inter-linked markets (e.g., credit and labour). To that effect, the project has adopted the following definition:

Economic bonded labour is a situation where the dominant position of an employer on the market of financial services and/or on other vital markets induces an important level of exploitation on the labour market, characterized by compulsory work against quasi-discretionary retribution.

Causes of Debt Bondage

An important aspect of preventing debt bondage is to identify families in bondage as well as those at risk of becoming bonded. Research undertaken by the project has determined, not surprisingly, that the overwhelming reason for a family to become bonded is poverty, understood as lack of access to and control of their livelihood and a high degree of vulnerability to risks. But poverty alone is not a sufficient indicator. To assess the vulnerability of a person or household to fall into bondage, the following factors were identified as important:

Social exclusion. Social and cultural factors, like the caste system in India and Nepal, can cause or reinforce bondage. Preliminary findings and observations from the field suggest that families who face social exclusion because of religion, ethnicity or caste

are significantly more vulnerable to labour exploitation and debt bondage than other economically poor families. Similarly, migrant labourers and families without local social networks are also vulnerable to exploitation and debt bondage.

Asymmetric information. Project baseline studies revealed that families who are vulnerable to bondage are generally illiterate. Field observation suggests that an inverse correlation exists between a family's understanding of its contractual relationships with the employer (e.g., the terms of remuneration, interest rates on employer loans) and its vulnerability to bondage. Illiteracy and lack of numeracy allows employers to manipulate the credit and wage accounts with an intricate system of advances, payments in kind and hidden interest rates.

Multiple roles of employers. The multiple social and political roles of employers (or their relatives) in the community increase the vulnerability of labourers to exploitation. Direct or indirect influence in locally elected bodies and/or in the law and order system (police, judiciary) allows employers to prevent labourers from taking legal action.

In-kind linkages. In-kind remuneration allows employers to hide low wage levels. For example, workers' remuneration package may include food, security, shelter, clothing, health or other essentials. In-kind compensation promotes dependency, whereas monetary benefits would allow workers to make basic life choices themselves. This dependency also gives a greater leverage to an employer's threats than a possible cut in wages.

The reasons behind the decision of the employer to opt for a bonded contract are also crucial to understand the incidence of bonded labour, but little is known about employer motivations. In contexts of quasi-monopolies, of absence of law as a real deterrent, and of workers' poverty, the employer is ultimately the main player to influence the incidence of bonded labour. Current project research in Nepal focuses on the economic reasoning of the employers to choose such contracts, the analysis of the environment in which some employers decided to move away from bonded labour contracts to daily wage based ones, and the feasibility to reproduce such environments. Empiric observation in the region shows that employers' motivations for choosing bonded labour contracts include a) more profit, b) ensuring the presence of labourers at a reduced price during the peak seasons, c) rent seeking behaviour (e.g., for absentee landlords), and d) maintaining a vote bank.

Towards a “Worst Forms Approach” to Bondage

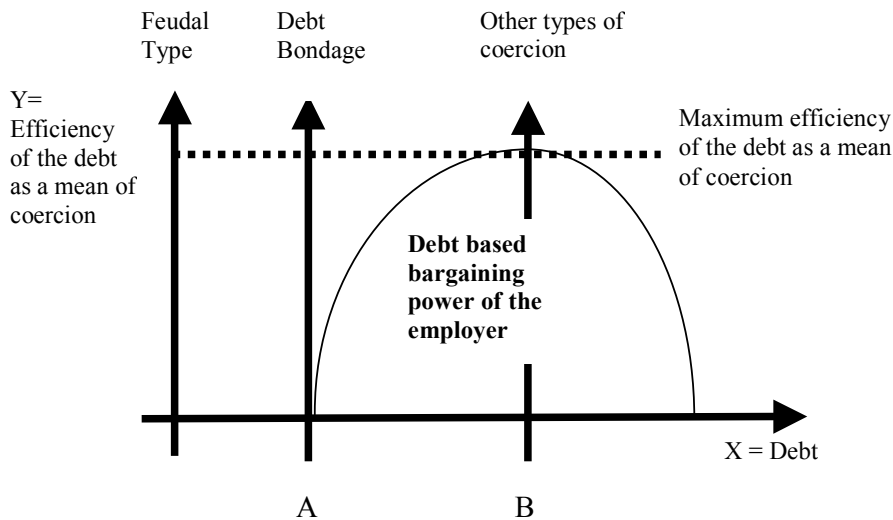
Bonded labour can assume many forms with a variety of degrees of severity. Bondage arrangements can be temporary or (quasi-) permanent. Bonded labourers may work for an employer year round or they may only have an obligation to give the employer preference in peak seasons.

Bondage itself is not linked to the duration of contracts. One can be bonded for a month or for a lifetime—one can even inherit a bondage status. However, there is a dynamic relation between indebtedness and labour contracts that are likely to make the latter increasingly exploitative as the debt increases. Exploitation can also adapt to environmental, economic or policy changes. In Nepal after abolishment of the Kamaiya-system, for example, bonded labour contracts became conditional sharecropping agreements where wives and children have to work for free.

The conjunction of a labour and a credit contract is not however sufficient to define bonded labour and one needs to qualify the nature of the resulting exploitation. Bondage relations can occur as a result of traditional or social customs, but even economic bondage is not exclusively based on inter-linkages between the labour market and the credit market. Inter-linkages between the labour market and other markets, particularly for basic needs such as shelter, food and water, can lead to bondage. In Nepal, for example, studies showed that in some districts less than half of the Kamaiya families were indebted to their employer. But because families lacked houses and land, they were dependent on landlords for shelter and food, similar to a feudal relationship.

Bondage could therefore be depicted as a continuum, such as shown in Figure 1. In feudal like situations, the credit link is not needed because the worker “belongs” to the employer. At the other extreme, above a certain level of the debt, the employer no longer expects to recover the loan, while the labourer knows that he/she can never repay the debt. In such a situation, the use of debt to apply pressure to a labourer becomes less effective and an employer may resort to other types of coercion, such as violence and restrictions on the freedom of movement.

Figure 1: Efficiency of Tactics to Coerce Bondage



Accordingly, perceived advantages and disadvantages of bonded labour vary according to the periods:

	Advantages: Between A and B	Disadvantages: Beyond B
Employer	<ul style="list-style-type: none"> • Employee will stay during peak season 	<ul style="list-style-type: none"> • Less productive • Loss of investment (credit will not be repaid) • Loss of control through debt
Employee	<ul style="list-style-type: none"> • Labour guarantee • Advance (not always repayable) • Informal safety net 	<ul style="list-style-type: none"> • More violent • New forms of exploitation • No escape • No private life • No bargaining power

This continuum helps to establish a distinction between the worst forms of bondage—which could be defined based on the length of the contracts, working conditions and limitations in freedom of movement—and milder forms that labourers enter temporarily as a risk adverse strategy or for the improvement of their living standards. In one less exploitative form, the employer uses debt element to guarantee labour availability during peak seasons while labourers are secured of their daily meals in slack seasons. Certain villages in Andhra Pradesh recently showed an increased incidence of one year bonded contracts against which the labourer was able to secure an advance needed to build a house.

There may be a progression from the milder forms of bondage towards the more exploitative types. This distinction is important because the programming approaches could be quite different if the project targets families who got a salary advance and are paid below market rate for a limited period, and those that suffer from severe exploitation, without any hope to escape. Although strict enforcement of legislation would be an obvious strategy for the latter sort, in both cases the position and attitude of the bonded labourers themselves should be taken into account before any action is taken. Legal provisions for India and Pakistan for instance include the necessity for the labourer to testify during legal procedures of release. It may be that a “rescue from bondage” results in exclusion from access to essential resources and services in the community. Release without the availability of livelihood alternatives may force a family deeper into destitution.

Regarding microfinance, the project in principle does not provide credit to bonded families for repayment of their debt as it undermines law implementation (bonded debts are illegal). On a larger scale, this strategy would also create a market for bonded debts, which could sustain the existence of bondage. The repayment capacity of families may be also further undermined, as now two loans have to be repaid at the same time.

The real-life situation is however not that clear-cut. Already a number of clients of microfinance institutions (MFIs) are de facto bonded, without MFIs being aware of that fact. In some cases, NGOs purposefully provide loans to bonded labourers to buy their freedom. The following justifications are given by NGOs/MFIs or by bonded labourers themselves:

1. Whether the level of exploitation is relatively severe or mild, offenders of national bonded acts are rarely prosecuted and punished. As payment below minimum wage is a fact of life in many rural parts of South Asia, members of the community would generally even oppose strict punishment of employers in the relatively milder form of bondage.
2. The employer is sometimes the only reliable provider of work for vulnerable families, who do not want to jeopardize their only livelihood source by denouncing their employer. Rather, a family member would become member of a MFI to generate an additional income source and better manage the family’s cash flow.
3. The real level of indebtedness depends on the capacity of a creditor to enforce repayment. Debts of former Kamaiyas, for instance, have been declared illegal and are officially nullified. However, discussions with former Kamaiayas revealed that they felt having no other choice than to continue repaying their old loans again as soon as the employer would claim them. As a consequence, the level of indebtedness is difficult to fully ascertain in many cases, and MFIs are not in a position to judge whether their clients are bonded.

4. In Bangladesh, there is no legislation against debt-bondage and therefore this discussion, however valid, does not take place among microfinance providers.

Saving and credit groups under the project include members of bonded labour families, but do not encourage repaying debts to employers through the project’s microfinance services. In practice, it is not always possible to monitor exactly for what purposes financial services are used, nor may it be in the best interest of the bonded family to keep these two different types of financial relations completely separate from each other.

Operational Insights: Project Implications

Although the South Asian Project for the prevention of Debt Bondage has been in full operation for less than two years, it already has learned a number of useful lessons, as discussed below.

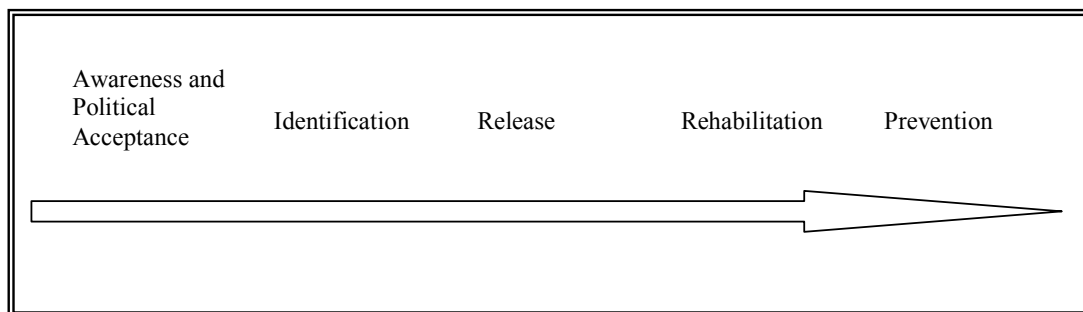
Targeting Families rather Children

The original project title, “Children as Collateral,” reflects the initial emphasis on bonded child labour. In most cases, however, children are not kept in bondage separately from their parents but the entire family is bonded and children work for a nominal remuneration alongside their parents. In cases where children work in bondage away from their family (e.g., domestic work), it was the family situation and a decision made by adult family members that resulted in giving a child away in bondage. In other cases children can inherit debt from parents. As a consequence, the approach of the project to prevent child bondage needs to be based on interventions that impact the whole family situation. A “child only” approach will not be effective because core problems in the family (e.g., lack of income, food insecurity) would not be addressed.

Prevention versus Rehabilitation

There are five different types of interventions necessary to eradicate debt bondage, as summarised in Figure 2. First, there is a need for policymakers to accept that indeed debt bondage is an issue about which they should be concerned, and then to create an appropriate legislative and legal environment. The second intervention is to identify bonded labourers and then to use the legal system to release them. The fourth step is to rehabilitate released labourers. The final intervention is to create conditions in the labour and credit markets to prevent debt bondage.

Figure 2: Five Areas of Interventions against Bonded Labour



The project was originally conceptualised to focus on the fifth area, the prevention of debt bondage, with some additional work on broadening awareness and political acceptance. The situation in Nepal and Pakistan, however, has allowed the project to also consider the issue of rehabilitation. In Nepal the cabinet decision in July 2000 to abolish the Kamaiya system led many families to leave the employer's land. In Pakistan, bonded labourers that escaped or were freed from bondage settled in a number of camps near Hyderabad. In both cases the families possessed next to nothing and were in urgent need of support. NGOs and government provided some immediate aid such as food and temporary shelter. Medium-term support (e.g., skills training, education for children, access to employment) required for a sustainable socio-economic rehabilitation of these families was severely lacking.

Both in Nepal and Pakistan the Government suggested that the project should address the problems of former bonded labourers, as it was realized that without support for a sustainable rehabilitation former bonded labourers are highly vulnerable to relapse into bondage. This risk is confirmed by discussions with former bonded labourers in Nepal which revealed that in spite of the fact that their debts were extinguished in July 2000, many families have become highly indebted again, some to their old landlords. The project, therefore, also focuses on rehabilitation of former bonded labourers in Pakistan and Nepal.

Experience so far has shown that the start-up of activities with families who are released from bondage takes longer than for families vulnerable to bondage as former bonded labourers:

- are generally used to a higher level of dependence on others;
- often lack self-confidence to enter a development process;
- have no experience of participating in group processes;
- find it difficult to trust outsiders, including NGOs trying to support them;
- suffer from a higher level of social exclusion;
- have had (even) less access to education; and
- have fewer assets to fall back on.

Financial and Non-financial Interventions

Most professional MFIs in South Asia do not work with the poorest segments of the population, but rather focus on the market that is a little better off, sometimes referred to as the "middle poor". This situation is partly explained by sustainability arguments from MFIs that are concerned about higher default risk and the transaction costs for smaller loans. The group selection process is also a contributing factor since members exclude the poorest community members who represent a threat to the cohesion and stability of the group. The poorest of the poor are also known to opt out of participation or quickly drop out because their irregular cash flow is not suited to the MFIs' strict repayment conditions. Consequently, families vulnerable to bondage, which are typically among the poorest part of the population, do not usually have access to MFI loans.

Although microfinance is at the core of the project's interventions to prevent debt bondage, complementary services are required for sustainable reduction of vulnerability to bondage. Project studies and experience confirm this perspective and even strengthen the perception that without social empowerment escape from extreme poverty is unlikely. Without a certain level of bargaining power, discrimination and exploitation will prevail. Without social awareness, high unproductive expenditure (e.g., ceremonies, dowry, alcohol) may offset any increase in income.

The project, therefore, has adopted an integrated and process-based approach in which target families are motivated to form groups. Social and economic empowerment initiatives are provided to groups, with the idea that being a member by itself and learning to function in a group will raise members' confidence and contribute to empowerment of target families. At the same time, group members are also taught basic literacy and numeracy skills, and are trained to manage their own savings, to lend from their own savings and, eventually, link-up with MFIs, banks or other financial service providers to access external funds.

The process of economic empowerment is strengthened by the provision of vocational training, skills and entrepreneurial training, although it is too determine the impact of this support. It is realized, however, that increased and more reliable income sources are crucial for sustainable reduction of vulnerability, and that standard approaches may not be sufficient. For instance, identification of skill training should not be based only on the often insufficiently informed wishes of the trainees and/or on the availability of trainers on the local market, but on thorough research on market opportunities for alternative livelihoods.

Theoretically, interventions can be divided in microfinance and non-financial services, and an MFI could have been contracted exclusively for the delivery of microfinance. In practice, however, in all four countries multi-purpose NGOs (providing both financial and non-financial services) emerged from a competitive selection process as the most appropriate implementing partners (see Table 2). In a more advanced stage, however, mature groups may be linked with professional MFIs to circumvent possible limitations of the multi-purpose NGOs in terms of institutional capacity or legal status (e.g., restrictions to collect savings).

Table 2: Implementing Partners in the Prevention of Debt Bondage

Area	Sector	# Clients	Partners
Bangladesh, Tangail	Sex workers	100	Society for Social Services (SSS)
Bangladesh, Tangail	Weavers	275	Society for Social Services (SSS)
Bangladesh, Sirajganj	Agricultural workers	375	Thengamara Mohila Sabuj Sangha (TMSS)
India, Andhra Pradesh, Ranga Reddy District	Agricultural workers	1020	Ankuram Sangamam Puram (ASP)
India, Tamil Nadu, Terivellure District	Agricultural workers	2000	Integrated Rural Development Society (IRDS) and Madras Social Service Society (MSSS)
Nepal, Banke District	Agricultural workers (mainly former Kamaiyas)	985	Mahila Upakar Munch (MUM) and Rural Reconstruction Nepal (RRN)
Pakistan	Agricultural workers (former Haris)	820	National Rural Support Programme (NRSP)

An important lesson so far is that the synergy between the different project services depends on the capacity and previous experience of the implementing partners. While there are clear differences in their capacity, even the more experienced partners are best at replicating methods with which they are used to working. The project has been acknowledged by the partners as an opportunity to exert more creativity and to boost their institutional capacity for experimentation and change.

Similarly, there are limitations to the technical and managerial capacity of ILO project staff, both in time and expertise. Although all staff have relative strengths, the combination of

managerial, political, social, communication and technical skills in terms of microfinance, group processes, social awareness, education, health, social rehabilitation, enterprise development, etc. may be too much to expect in one person. Contracting of additional short-term (external) technical expertise can therefore become a crucial input for a project with a multi-faceted integrated approach that aims to develop high quality services.

Diverse Financial Services

The financial needs of the target groups are different from regular microfinance clients. While other clients often look for loans for productive investments, families vulnerable to bondage are particularly in need of financial services to smooth income and expenses, to manage risks, and possibly to pay for social obligations. In addition to these services, families may also desire to access income-generating loans, but the structure of most of these loans is not suitable for the poorest segments of the market, which are characterized by irregular and unpredictable income flows.

Most risks that are not part of life-cycle events are unpredictable, like floods, illnesses and death of family members. Their unpredictable nature suggests that insurance may be an appropriate intervention as well. The project is also tasked with the challenge of reducing expenses for life cycle events, such as marriage and religious ceremonies, through appropriate awareness raising.² As a consequence, the project is not promoting targeted savings products for marriages and dowries. Targeted savings for house-repair or other specific purposes are possible, as long as savings are not blocked in case emergency expenditure is required.

Involving Employers

As the project has progressed, it has become clear that the involvement of employers is crucial in areas with a large labour supply and limited employment opportunities. A liberation of all bonded labourers without access to alternative employment is not a solution for the bonded families. Employers, on the other hand, may resort to one of the following alternatives, which do also not improve the employment situation:

- Stop production
- Contract other (migrant) labourers on a similar basis
- Replace labourers through mechanization

The project has, therefore, started to study financial and labour markets from the perspective of employers and will invite a number of them to take part in small demonstration projects to try out alternatives to bonded labour arrangements. These pilots are intended to secure the continuity of employment for labourers, with improved conditions, while providing examples of economic substitutes and “good conduct” to other employers.

This approach of course needs to be balanced with the threat of prosecution in cases of severe exploitation, as provided for under national laws. However, a “rights-based” approach in which employers are stigmatized as offenders may have a more limited impact than an approach based on dialogue with employers. One example is to bring more attention to certain social and moral values that may exist in society that would denounce exploitation of fellow community members. Through awareness raising and providing certain incentives, incidence of the worst forms of exploitation may be considerably reduced. This softer

² The same applies for awareness raising on alcohol and drug consumption

approach however may only be effective if it is accompanied by a credible enforcement of the law.

Policy Impact

Finally, the project has placed considerable emphasis on dialogue and building trust to make an impact at the policy level. Although other factors influenced a general trend towards more openness on bonded labour in South Asia, the project has contributed to positive changes in Government attitude on the subject, as indicated in Table 3.

Table 3: Policy Changes regarding Debt Bondage: 2000-2002

	Situation 2000	Situation 2002
Nepal	<ul style="list-style-type: none"> • Kamaiyas freed on 17th July without rehabilitation plans 	<ul style="list-style-type: none"> • Comprehensive rehabilitation plan drawn • Kamaiya Act adopted • Informal recognition of Kamaiya-like situations beyond the group identified
India	<ul style="list-style-type: none"> • No technical cooperation project on bonded labour 	<ul style="list-style-type: none"> • Approval of first technical cooperation project on bonded labour by Central Government • Invitation by 3 States to initiate activities: Andhra Pradesh, Tamil Nadu and Karnataka • All 3 State Governments have committed to contribute 20% to the budgets of bonded labour projects
Bangladesh	<ul style="list-style-type: none"> • Existence of bonded labour not recognized 	<ul style="list-style-type: none"> • Concept of Indebtedness linked to labour exploitation accepted • Recognition of the need to undertake research on the subject
Pakistan	<ul style="list-style-type: none"> • Bonded labour sensitive topic 	<ul style="list-style-type: none"> • National Action Plan Against Bonded Labour adopted